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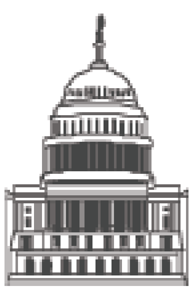


FEBRUARY 28, 2002

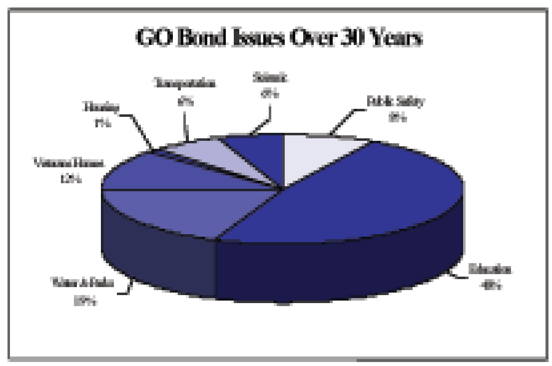
SENATOR BILL MORROW

CAPITOL UPDATE

THE STATE'S INDEBTEDNESS

Here are the facts about California's current financial situation concerning general obligation bonds and how they effect our economy. Bonds are commonly referred to as "debt financing" because they are used to balance the state's budget when there is a revenue shortfall. However, California's budget already contains a large amount of debt and may not be able to prudently support additional debt.

G.O. BOND ISSUES OVER 30 YEARS	
Public Safety	$4,087,000,000
Education	$23,035,000,000
Water & Parks	$9,046,000,000
Veterans	$5,660,000,000
Housing	$650,000,000
Transportation	$2,990,000,000
Seismic Safety	$2,800,000,000



DIFFERENT KINDS AND USES OF DEBT

Cost Comparison for a $100 Million Project	
Pay-As-You-Go	$100 million
G.O. Bonds (20-year)	$167 million
Lease Revenue Bonds (20-year)	$190 million

General Obligation Bonds: The State Constitution prohibits the creation of "general obligation" indebtedness of the State unless a bond law is approved by a majority of voters. General obligation (G.O.) bond acts provide that debt service on G.O. bonds shall be appropriated annually from the General Fund, and all debt service must be paid before any other state obligation. Typically, G.O. bonds fund long-term, capital-intensive construction projects.

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Revenue Bonds: The state also uses lease-revenue bonds to supplement the G.O. bond program. Under this method of financing, budgeted lease payments are used to pay off principal and interest charges on bonds. The lease revenue bonds are typically more costly than G.O. bonds. Historically, lease revenue bonds have been used to fund certain construction projects that have a distinct revenue stream, such as rent or lease payments.

[Note: In this year's budget, the Governor proposes to use lease revenue bonds in a much different manner. Each year, the state receives $400 million from the tobacco settlement. The Governor proposes to engage in leverage financing with some of the revenues California will receive over the next 22 years. While that allows the state to borrow and spend $2.4 billion in the current year, it is a scheme that requires that we tie-up close to $200 million each year for the next 22 years for debt repayment. Ultimately, it means that we trade $2.4 billion today for $4.2 billion paid over the 22 years of debt.]

HOW MUCH DEBT IS TOO MUCH DEBT?

Outstanding Debt	$26,730,848,000
Authorized, But Not Yet Issued	$9,263,075,000
TOTAL	**$35,993,923,000**
Annual Payment in 2001-02	***$3,185,963,918***

The state currently has $36 billion in outstanding bonds and bonding authority upon which we pay $3.2 billion annually in interest and principal. This results in a ratio of $1,006 of *authorized* state debt per California resident.

Of the $3.2 billion in state debt payments paid this year, almost half, or $1,475,498,144, was spent on interest payments alone.

WHAT COULD WE BUY WITH THE $1.475 BILLION INSTEAD OF PAYING INTEREST?
Purchase over 30 million new textbooks for our schools
Or, hire 21,000 new teachers
Or, fund *all* of the water storage construction projects of the state-federal water program known as CALFED
Or, hire 16,000 new police officers

For every $1 billion in General Obligation debt the state incurs, we increase the annual cost to taxpayers by approximately $85 million.

While we are facing a significant budget shortfall this year, during the three previous years, the state increased spending by more than $20 billion. Rather than investing the surplus dollars on building roads and schools, new state programs were established and bureaucracies expanded. Therefore, due to the expansion of government programs, vital infrastructure programs have forced the state to employ expensive debt financing to fund the capital needs of our state:

1998	School Facilities	**$9.2 billion**
2000	Clean Water	**$1.97 billion**
2000	Parks	**$2.1 billion**
2000	Libraries	**$350 million**
2000	Veterans Home	**$50 million**

DEBT FINANCING CURRENTLY BEING CONSIDERED

The Governor's proposed budget includes a significant change in the use of debt financing by borrowing from fund sources of tomorrow to pay for the operating expenses of today. This is in addition to the $6 billion in energy bonds which the state is poised to sell in the next several months. When sold, they will obligate 15 years of payments for the electricity purchased last year as a result of poorly negotiated contracts by the state. Furthermore, the Governor and Legislature are considering additional General Obligation bonds (on top of the $2.6 billion Park Bond Act and $400 million voter technology bond which will go before the voters in March of this year).

In December, Governor Davis announced his support for a school bond package that would authorize $30 billion in school bonds. Under the Governor's proposal, the Legislature would, with a single legislative vote, place a $10 billion school bond on the ballots in 2002, 2004, and 2006. An alternative proposal is being considered that would authorize $24.5 billion in bonds over the next two election cycles. Additionally, the Legislature will consider this year a $2 billion housing and homeless bond and a $2-3 billion water bond. Increasing the state's debt ratio with these measures could bring our *annual* debt costs to well over $8 billion. (For more information on the school bond discussions see http://republican.sen.ca.gov/opeds/14/oped1180.asp)

While investment in the state's infrastructure is vital, the magnitude of the potential debt is significant – the possibility of doubling our outstanding debt authorization with another $35 billion in bonds. The Legislature, Governor Davis and voters must decide whether to commit future generations of Californians to 20 or more years of multi-billion dollar debt financing. It's a commitment that should not be entered into lightly.

Order to Double gas prices?

http://www.energy.ca.gov/mtbe/2002-02-19_STILLWATER_RPT.PDF

A recent analysis by the state's Energy Commission released Tuesday, February 19th, indicates that Davis' MTBE-replacement deadline would create a shortage of gasoline. The price of California's gasoline will double at the pump if Gov. Gray Davis keeps his order to eliminate the environmentally troublesome MTBE additive by the end of this year. In an economic analysis commissioned by the Davis administration, the oil refinery consulting firm Stillwater Associates said the governor should postpone the MTBE ban to November 2005. Prices will move in the range of $2 to $3 per gallon when crude- oil pricing and refinery operations would normally have resulted in pricing around $1.50 per gallon. To read the Energy Commission's analysis go to:
http://www.energy.ca.gov/mtbe/2002-02-19_STILLWATER_RPT.PDF

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